

Michael J. Cuggino President & Portfolio Manager, *Permanent Portfolio Family of Funds*

Comments & Outlook

The US economy has been in maintenance mode. Companies have been doing just enough to keep up—replenishing inventories and curtailing spending. As a result, the short-term outlook continues to be somewhat negative. But the US economy has a strong foundation with untapped potential and available liquidity to drive future growth.

I'm cautiously optimistic about the future. Corporate profits remain strong, even in this period of decreased economic activity. By and large, US corporations continue to make money, and many firms are sitting on large cushions of cash they've built up by forgoing extra spending and reinvestment. In addition, unemployment remains high, and there's a tremendous amount of slack in the labor market. Both of these factors will allow companies to grow and expand once they decide to do so.

Recommended Strategies

We look for companies that can preserve and increase pricing power on their goods and services. We also like names that maintain, control or reduce their cost structures over time.

What to Buy Now

The financial-services sector hasn't performed as well as the overall market. But we can't have consistent and stable long-term economic growth without a strong, vibrant financial system. For the long term, financial stocks will be good investments.

Consider **State Street Corp** (NYSE: STT), a service provider to the asset management industry. As assets reflate and wealth continues to be stored away, State Street will return as a major player in this space.

State Street is an extremely efficient operator, and its stock trades at roughly 10 to 11 times earnings, a lower multiple than what we've seen historically.

Eventually, I expect the company to reinstitute a higher dividend.

FedEx Corp (NYSE: FDX) is the leader in transportation and shipping. The stock is a play on economic growth. Management recently announced positive guidance, a potential indicator of improving economic activity. FedEx has been able to maintain its pricing levels and has even increased its rates in some places.

Freeport-McMoRan Copper & Gold (NYSE: FCX) is a geographically diversified natural-resources company that primarily mines copper. The global economic growth story is intact. When this growth is combined with a weaker dollar, we expect copper prices and demand to remain strong over the long term.

This will allow the company to sell its assets and extract resources at profitable rates, resulting in higher revenue. ■

Stephen Goddard Portfolio Manager, *Touchstone Small Cap Core (TSFIX)*

Comments and Outlook

The economy is recovering gradually, though some areas are rebounding much more strongly than others. We see improvement across the board, with the exception of sectors related to the housing industry. The industrial and manufacturing sectors are having some of their best years in terms of margins and cash flow generation, benefiting from tight capacity and increased demand in developing regions, especially Asia.

Recommended Strategies

We prefer companies with strong market positions, consistent records of profitability and shareholder-oriented capital allocation. Often, these companies are underleveraged and can benefit more from the unusual debt-equity cost spread arbitrage in the marketplace today. These firms can create shareholder value by repurchasing their

undervalued equity with low-cost financing.

What to Buy Now

Corrections Corp of America (NYSE: CXW) is the dominant player in the private prison business and commands close to half of the industry's market share. As governments tighten budgets, Corrections Corp should benefit from increased outsourcing to alleviate the overcrowding in prisons.

Because the firm owns the majority of its prisons, it could convert its properties to a real estate investment trust (REIT) structure, which should significantly boost the valuation. Activist shareholders have proposed such an action, but management has not yet committed to the conversion.

Hawaii-based **Alexander & Baldwin** (NYSE: ALEX) has been in business for over 100 years and dominates

the Hawaii-Mainland cargo/container market through its main operating subsidiary, Matson. Matson benefits from the Jones Act, which creates high barriers to entry for new competitors, as well as additional shipping traffic from Asia. The firm hit a tough patch in 2008-09, when the economic downturn hurt Hawaii's travel-leisure economy. But fundamentals have begun to improve.

NewMarket Corp (NYSE: NEU) provides additives for fuel and lubricants and benefits from increasing global driving mileage.

The industry has undergone major consolidation, with only a fraction of the competitors that were in place in the 1980s and '90s still in the market. The survivors enjoy favorable pricing dynamics. NewMarket's margins have more than doubled over the past 12 to 18 months, providing exceptional free-cash flow growth. ■